

Message Text

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ACTION EB-08

INFO OCT-01 EUR-12 EA-10 NEA-10 ISO-00 SP-02 ICA-11
AID-05 NSC-05 TRSE-00 SS-15 STR-07 OMB-01 CEA-01
CIAE-00 COME-00 FRB-03 INR-10 NSAE-00 XMB-02
OPIC-03 LAB-04 SIL-01 L-03 PA-01 IO-13 /128 W
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FM AMEMBASSY ISLAMABAD
TO SECSTATE WASHDC 8759
INFO AMEMBASSY MANILA
AMEMBASSY PARIS

C O N F I D E N T I A L ISLAMABAD 8214

MANILA FOR ADB; PARIS FOR USOECD

EO 11652: GDS
TAGS: EAID EFIN PK
SUBJ: DEBT RESCHEDULING

REF: ISLAMABAD 8162

1. SUMMARY: PAKISTAN HAS JUST REITERATED ITS DESIRE FOR DEBT RESCHEDULING AND CALLED FOR A MEETING TO DISCUSS IT. IT STILL DOESN'T URGENTLY NEED RESCHEDULING, BUT IT DOES HAVE AN UNDERLYING STRUCTURAL PROBLEM AND ITS WORKERS' REMITTANCE-SWOLLEN FOREIGN EXCHANGE RESERVES WON'T STAY AT PRESENT LEVELS FOREVER. WE SUGGEST WE SEIZE THE OPPORTUNITY PRESENTED BY THE RESCHEDULING REQUEST TO WORK ALONG WITH THE BANK AND FUND TO GET THE PAKISTANIS TO REFORM THEIR ECONOMY IN RETURN FOR RESCHEDULING OR ITS RESOURCE-TRANSFER EQUIVALENT. OTHERWISE WE MAY BE FACED WITH A CRISIS LATER AND A SURPRISE-FILLED DEBT MEETING -- IF IT TAKES PLACE AS WELL IT MAY. THE SURPRISES COULD HAVE A LESS PLEASANT OUTCOME THAN THEY DID IN PARIS IN JUNE. END SUMMARY.

2. THE REFTTEL CONTAINED THE TEXT OF A NOTE VERBALE FROM THE
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ECONOMIC AFFAIRS DIVISION, GOVERNMENT OF PAKISTAN, CONCERNING PAKISTAN'S DESIRE THAT A MEETING TO DISCUSS THE DEBT SITUATION BE HELD BEFORE THE END OF 1978. IT IS APPARENT FROM THIS NOTE AND FROM WHAT GOP OFFICIALS TELL US THAT PAKISTAN WAS NOT DAUNTED BY THE COLD RECEPTION ITS REQUEST FOR DEBT RESCHEDULING MET WITH AT THE PARIS CONSORTIUM MEETING LAST JUNE. PAKISTANI OFFICIALS CONTINUE TO FEEL PAKISTAN HAS A STRUCTURAL DEBT PROBLEM AND THAT

THE RECENT INCREASE IN FOREIGN EXCHANGE RESERVES IS SOLELY THE RESULT OF INCREASED WORKERS' REMITTANCES. THEY LOOK UPON WORKERS' REMITTANCES AS AN UNDEPENDABLE AND PROBABLY TEMPORARY UNDERPINNING FOR THE BALANCE OF PAYMENTS AND AS ONLY TEMPORARILY MASKING THE STRUCTURAL PROBLEM.

3. WE THINK THIS ANALYSIS HAS MUCH TO RECOMMEND IT. WHILE PAKISTAN IS NOT NOW IN AN "IMMINENT DEFAULT" SITUATION, IT IS HIGHLY PROBABLE THAT ITS BALANCE-OF-PAYMENTS SITUATION WILL AGAIN WORSEN IN THE NOT-TOO-DISTANT FUTURE. IT IS BETTER THAT BOTH WE AND THE PAKISTANIS PLAN FOR THIS CONTINGENCY NOW AND NOT WAIT FOR IT TO OVERTAKE US.

4. IT IS ALWAYS POSSIBLE THE DECEMBER MEETING WILL NOT TAKE PLACE BECAUSE THE PAKISTANIS WILL NOT BE ABLE, ESPECIALLY WITH AN INTERIM GOVERNMENT, TO MAKE THE SORT OF BINDING COMMITMENTS THAT WOULD MAKE THE BANK AND FUND AND OTHER DONORS THINK THE MEETING WORTHWHILE. WE THINK IT IS BEST TO PROCEED ON THE ASSUMPTION THE MEETING IS LIKELY TO TAKE PLACE. WE ALSO THINK IT BEST TO PROCEED ON THE ASSUMPTION THAT THE NUCLEAR REPROCESSING ISSUE WILL BE BEHIND US BY THEN. IN OUR JUDGMENT, THE UNITED STATES SHOULD NOT FOCUS SOLELY ON PAKISTAN'S CURRENT LEVEL OF FOREIGN EXCHANGE RESERVES, BUT ALSO ON HOW THEY MAY BEST BE HUSBANDED WHILE PAKISTAN MAKES THE FUNDAMENTAL ECONOMIC CHANGES NEEDED TO GET ITS ECONOMIC DEVELOPMENT PROCESS MOVING AGAIN AND MOVING IN A MANNER THAT IS CONSISTENT WITH THE RESOURCES LIKELY TO BE AVAILABLE TO

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IT. THEIR RESERVES ARE A CUSHION THAT CAN BE USED TO BUY SOME TIME BUT THEY SHOULD BE USED WISELY AND NOT MERELY ALLOWED TO ERODE AWAY. IT SHOULD BE MADE CLEAR TO THE PAKISTANIS THAT THEY WILL HAVE TO COME TO THE NEXT MEETING BETTER PREPARED THAN THEY WERE WHEN THEY REQUESTED MASSIVE FOOD AID THIS SUMMER. IT MUST ALSO BE MADE CLEAR THAT THEY MUST DEMONSTRATE POLICY SHIFTS IN PLACE THAT GIVE A GOOD HOPE OF TURNING THINGS AROUND AND NOT CONTENT THEMSELVES WITH ASSURING US ONE MORE TIME THAT THE POLICY STEPS WILL BE TAKEN. THE APRIL 7 WORLD BANK REPORT IS FILLED WITH CONCRETE STEPS THEY MIGHT TAKE. WE SHOULD WORK CLOSELY WITH THE BANK AND FUND TOWARDS EFFECTIVE REFORM WITH THE UNDERSTANDING THAT SUCCESS MEANS THE UNITED STATES WILL BE FORTHCOMING IN EITHER PARTICIPATING IN A GENERALIZED DEBT RESCHEDULING OR (IF THIS IS NOT POSSIBLE) FINDING OTHER EQUIVALENT MEASURES THAT WILL PERMIT US TO MAKE A CONTRIBUTION COMMENSURATE WITH OUR PAST ROLE IN ECONOMIC ASSISTANCE TO PAKISTAN.

5. BASED ON THE ABOVE, WE THINK THE USG'S RESPONSE TO THE NOTE VERBALE SHOULD NOT REJECT A MEETING TO DISCUSS PAKISTAN'S DEBT AND STRUCTURAL BALANCE OF PAYMENTS PROBLEM BUT SHOULD POINT OUT THAT THE ROLE THE PARIS CONSORTIUM MEETING GAVE FOR DECIDING ON A MEETING TO THE BANK AND THE FUND. THE RESPONSE MIGHT GO ON TO SAY

WE SHALL BE IN CLOSE COMMUNICATION WITH THE BANK AND THE FUND ON WHETHER THE SUGGESTED MEETING IS WARRANTED AND SHALL BE GUIDED IN OUR ATTITUDE AT ANY SUCH A MEETING BY THE FINDINGS OF THE BANK AND FUND ON PAKISTAN'S ECONOMIC POLICIES AND PROSPECTS. THE RESPONSE MIGHT ADD OUR UNDERSTANDING THAT THE FUND PLANS TO SEND A SPECIAL TEAM TO PAKISTAN IN THE FALL TO STUDY PAKISTAN'S ECONOMIC SITUATION AND THAT ITS FINDINGS MAY HAVE A BEARING ON THE PROPOSED MEETING.

6. WE THINK SERIOUS PREPARATION SHOULD BEGIN PROMPTLY. WE DOUBT THAT THE PAKISTANIS WILL GIVE UP EASILY ON THE NOTION OF A DEBT MEETING AND THE US SHOULD START EXCHANGING VIEWS WITH THE BANK AND FUND, AND WITH OTHER DONORS, SO THAT WE --AND OTHER PARTIES-- WILL BE READY WHEN AND IF IT DOES TAKE PLACE. OTHERWISE WE RISK CONFIDENTIAL

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ANOTHER SURPRISE-FILLED MEETING AND WE MAY NOT BE AS LUCKY IN THE OUTCOME AS WE WERE IN PARIS IN JUNE.
HUMMEL

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NNN

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